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Causes of Small Business Failure in Uganda: A Case Study from Bushenyi and Mbarara Towns [1]

CHARLES TUSHABOMWE-KAZOOBA

Abstract: The privatization drive and the Civil and Public Service reforms that began in the early 1990s in Uganda laid a foundation for an increased number of small business enterprises. By 2002, small scale enterprises were employing approximately 2,000,000, and serving about 6,000,000 people at business and household level. The entrepreneurs that set up these enterprises lacked business management skills and capital, and as such, many of them faced a number of problems, most of which were of a startup nature. A survey was carried out to establish the causes of small business failures in Uganda using businesses in Mbarara and Bushenyi towns as case studies. In-depth interviews and questionnaire methods were mainly used to collect data from 133 small business enterprises. It is concluded that the causes of small businesses failure are multidimensional and diverse. They include poor management as well as political, economic, social, cultural and environmental factors. In practice, many of these are interrelated. The survey revealed that the startup factors posed a greater threat than those that are encountered once the business has been established. As such, business people who successfully negotiate the initial startup hurdles have greater chances of future success in their businesses. Despite the solutions sought over the years, the business community in Uganda is still hampered by the challenges. The study concludes by making a number of practical suggestions against business failure.

INTRODUCTION

The privatization drive, which started in the early 1990s, made the Government of Uganda relinquish its position as the number one employer. The Civil and Public Service reforms downsized the public service, reducing staff employed by central government from 320,000 in 1990 to 191,324 in March 2001, a reduction of 40.9%.[2] As a result, tens of thousands of retrenched civil servants joined the private sector as small scale business owners. This led to the mushrooming of small scale business enterprises, most of which employed fewer than five persons and as many as 90% of the non-farm private sector workers. Since then, the number of small scale businesses in Uganda has grown from 800,000 in 1995 to about 2,000,000 in 2002. These serve about 6,000,000 people at business and household level of the 26.3 million population.[3]

Small scale business is defined as one which is independently owned and operated, and not dominant in its field of operation.[4] It can also be defined in terms of sales volume and by the number of employees in the business. In Uganda, these businesses are very small employing up to a maximum of 50 people, who in most cases are members of the same family. They have working capital of less than USD 26,882 and revenue value of USD 5,376 - 26,882 throughout each year of operation.[5] In addition, they have an asset base of up to USD $25,000.[6] The major activities of small scale businesses in Uganda are farming, buying produce, market vending, catering and confectionery, shop keeping, second hand clothing, health/herbal services, secretarial services, telephone services, handicraft, transport, and many others. The majority of these operate in shared premises and are set up before they get licenses. Ownership and management is on family basis and as such has a small scale operation. It is labour intensive and skills are acquired on the job, often using adapted technology. According to John Keough, more than 50 percent of

Charles Tushabomwe-Kazooba is a Lecturer, in Management Science at Mbarara University of Science and Technology. He holds an MBA from the University of Birmingham Business School 1988 and is a Chartered Certified Accountant.

them fight an uphill battle from the start and fail in the first five years.[7] This is a common scenario for Ugandan small businesses, as most of them 'never celebrate their first anniversary.'

The purpose of this survey was to investigate the reasons for small business enterprise failure. Another reason for the survey was to determine the financial impact of "load shedding" to the businesses that use electricity as a source of energy. Case studies of businesses in two towns in Uganda were made and for the businesses studied, causes of failure and some practical measures suggested are outlined. This knowledge could help in mapping out strategies for solving the number of problems faced by these businesses, thereby contributing to poverty alleviation, one of the Millennium Development Goals (MDGs). A version of this survey is to be translated in the local languages in order to be available to a wider audience.

METHODOLOGY

Study area and population

This was a descriptive survey of the startup causes of business failure and other issues faced by small enterprises. Mbarara and Bushenyi are located in Southwestern Uganda. These are the district headquarters of Mbarara and Bushenyi respectively in what was formerly called Ankole region. The two districts neighbour each other. Bushenyi town has a population of 22,259 people of which 10,429 are male and 11,830 are female. It covers an area of 44 square kilometers. On the other hand, Mbarara town has a population of 69,208 people, of which 34,191 are male and 35,017 female.[8] The total land area of the town is approximately 51.47 square kilometers. The economic activities of both towns includes but is not limited to crop and animal farming and trade, trade in retail and wholesale, workshops of carpentry and metal fabrication, hotels and food kiosks, brokerage, brick making, water vending, telephone operating, lodging and bars, taxi operating and milk processing. Mbarara and Bushenyi have both informal and formal business enterprises. In most cases, they engage in the same products, reducing opportunities for internal domestic markets within the region. In addition, Mbarara has 9,171(5.7%) of the total national businesses and employs 19,946(4.4%) of the total national workforce. On the other hand, Bushenyi has 1,225(0.8%) businesses out of 160,883 in the whole country and employs 3,599 people. Most of these businesses fall in the category of trading.[9]

These two particular towns were chosen for three reasons: 1) because of their close proximity; 2) the observed increase of economic activity in terms of new buildings, schools, hotels, petroleum products gas stations; 3) viable small businesses have sprung up in the recent past in these towns but most of them have not survived for more than a year.

Data collection

Data was collected from 133 business enterprises by interviewing the owners. Of these businesses, 113(85%) were from Mbarara and the remaining 20(15%) from Bushenyi. The number of businesses in Mbarara compared to those in Bushenyi is in a ratio of seven to one, and this dictated the numbers chosen from each town. The numbers were also determined based on the numerous socio-economic activities in Mbarara compared to Bushenyi town. Businesses were chosen by random sampling, judgmental analysis, and partly purposive decisions in order to have a wide representation of business activities in the sample. Business activities that were similar in nature were grouped together for sampling purposes. Two methods were mainly employed in primary data collection. These are in-depth interviews and questionnaire methods.

Data from Bushenyi town was collected in two days and all the 20 respondents were interviewed with a research assistant who was taking notes of the proceedings of the interview. The duration of these interviews varied between one to two hours. For those in Mbarara town, data was collected mainly using a field-tested questionnaire. Both structured and unstructured questions were administered to the proprietors. A special questionnaire was designed to collect information on the financial impact of load shedding on businesses in Mbarara town. This was administered to the proprietors of gas stations, bars, saloons, computer training services, hotels, and milk coolers that accounted for 28(21%) of the respondents.

Data collected was cross-tabulated to show the different variables. The entry and analysis of data were done using Epi-Info version 6.04b statistical package. This generated frequency tables for socio-economic and demographic data, taking into account the relationship between independent and dependant variables of different enterprises. The qualitative data was collected, transcribed, and grouped. Double data entry and checking were used to minimize errors. Oral consent to participate in the study was obtained from all respondents. In addition, the researcher received approval from the town council leadership of Bushenyi and Mbarara.

FINDINGS

The response rate for the survey was high. One hundred thirty three (133) representing 95% questionnaires were returned out of the 140 distributed, of which 20(14%) were from the respondents in Bushenyi and the rest 113(81%) from Mbarara town. The high response rate was due to the fact that most of the questions were asked directly to the respondents. Of the responses received from the survey, 128 (96%) also gave suggestions on how they overcame common causes of business failure they encountered during startup or after they had established their businesses. These suggestions formed the basis for the practical action against business failure proposed in table 3.

Over ten different types of small businesses were sampled and studied from the two towns (see table 1). Of these businesses, 24(18%) were involved in general merchandise and 31(23.4%) were restaurants, hotels and bars. The other businesses studied were gas stations, milk cooling plants, maize milling, *jua kali* and saloons. Other activities studied included garages, hardware, clinics, pharmacies and those involved in selling second hand clothes. Also included in the study were business activities like security services and computer services (these are included under "others").

Table 1: Businesses studied by town

Business	Mbarara	Bushenyi	Total sample number studied n=133(%)
	Sample number studied (%)	Sample number studied (%)	
Filling stations/gas stations/petrol stations	10(7.5)		10(7.5)
Milk cooling plants	11(8.3)		11(8.3)
Restaurants, bars, hotels	28(21.1)	3(2.4)	31(23.4)
Maize milling	2(1.5)		2(1.5)
Garages	2(1.5)	1(0.7)	3(2.3)
Jua Kali	4(3)	4(3)	8(6)
General merchandise	18(13.5)	6(4.5)	24(18)
Saloons	10(7.5)		10(7.5)
Stationery	4(3)	2(1.5)	6(4.5)
Hardware shops		1(0.7)	1(0.7)
Pharmacy/clinic	5(3.8)	2(1.5)	7(5.3)
Others	19(14.3)	1(0.7)	20(15)
Total	113(85)	20(15)	133(100)

Source: Field data

The majority of the businesses studied were established after the 1990s, and these represented 124(93%). The turnover of these businesses 81(61%) ranged from USD 10,000 to 35,000. Only 4(3%) businesses had a turnover above this range. When asked what motivated them to go into the type of business, 69(51.9%) of respondents reported that they joined as a means of survival, 31(23.3%) as a need for self-employment, 11(8.2%) due to public demand. Other reasons cited were continuing the tradition, availability of market, success of others, no other options, fighting poverty, professional inclination and limited capital required. The number of people employed in each of these businesses is 5 and below, representing 104(78%). Only 29(22%) businesses employed more than 5 people but below 50. The majority of these were petrol stations, restaurants, bars and hotels.

Proprietors were queried whether they received business management training either before or after establishing their businesses. Of the respondents, 55(41%) had received training but most of these received training only after they had established the business. Of the 41% who had training, 18% respondents are those operating filling stations since it is one of the requirements by the petroleum companies to train their agents. The remaining 78(59%) of the respondents had not received training. Most of the business management training is conducted by the Ankole Private Sector Promotion centre based in Bushenyi town.

All the respondents reported a number of problems they have faced. The questionnaire had listed 13 alternatives of causes of business failure but they were given an opportunity to list others not included. The study revealed a number of reasons why small business enterprises fail that were categorized into internal and external factors. According to the respondents, taxation was the major problem. Among the respondents investigated, 70(53%) of them complained that taxation was contributing to the malfunction of their businesses (see table 2 for details).

Table 2. Causes of small business failure (n=133)

Ranking	**Internal factors**		**External factors**	
	Cause	Number (%)	Cause	Number (%)
1			Taxation	70(53)
2			Load shedding	67(50)
3			Lack of capital	64(48)
4			Poor market	48(36)
5			High rent charges	48(36)
6	Wrong pricing	47(35)		
7	Negative cash flow	45(34)		
8	Poor record keeping	44(33)		
9	Domestic and family situations	43(32)		
10			Delays in processing applications	41(31)
11	Management problems	35(26)		
12	Faulty product concept	32(24)		
13	Inadequate control of inventory	24(18)		
14	Lack of planning	23(17)		
15	Trouble among partners	19(14)		

Source: Field data

Other problems mentioned were load shedding 67(50%), lack of capital 64(48%), poor market 48(36%), high rent charges 48(36%), pricing 47(35%), negative cash flow 45(34%) and poor record keeping 44(33%). In all cases, recommendations were formulated to improve management of small businesses.

DISCUSSION

The aim of the survey was to investigate the causes for small business failures in Uganda. Many entrepreneurs (53%) reported that taxation is contributing to the malfunction of their businesses. With the introduction of Value Added Tax (VAT) in Uganda in 1997, many businesses have been hard-hit because of this category of tax. Given that the weight of this tax is borne by the consumer, this leads to an increase in price, which can dampen sales. The study also revealed that the local authorities impose other forms of taxation like ground rates, security fees, and trading licenses. Ground rate is a tax imposed on businesses according to the location and type of business facilities. These have a great impact on the operations of businesses. Another aspect of high taxation is a corresponding increase in illicit or illegal trade. Smuggled products have found their way into the markets of Mbarara and Bushenyi towns. These goods are attracting customers as they are sold at lower prices. This mitigates chances for the success of genuine business people.

Power shortages that lead to load shedding accounted for 50% of the respondents and high electricity bills were identified as major problems faced by businesses. The findings of the study revealed that on average, hotels, bars, filling stations each uses 582 units of electricity on a monthly basis which costs US $68. To make the situation worse, it was found out that on average, hydropower goes off 2 times a week for a period of 4 hours. Generators were found to be a major alternative source of power. Businesses that do not have generators come to a standstill during such times. Even those that use generators find it much more expensive because of the high costs of fuel (1-liter petrol costs USD 1.21). Thus, on average USD 216 is spent monthly on fuel for generators. A total expenditure of USD 284 on only electricity and fuel for generator is a substantial operational expense. Due to the expensive nature of generators, most businesses do not even have an alternative source of power. The situation is alarming when it comes to businesses that deal in milk cooling. When power is cut off at night and they do not have automated generators, their situation is worsened. In one night when power went off, an entrepreneur lost 580 litres of milk which had been bought on credit equivalent to USD116.

Power costs are high. East Africa has the most expensive electricity on the continent. $70 is charged per MWH in Kenya, $80 in Tanzania, and $46 in Uganda, yet the international standard is $40. South Africa has even managed $18.[10] The respondents pointed out that, with the privatization of Uganda Electricity Board (UEB), the costs of using electricity have increased and frequent power cuts have prompted the installation of alternative sources of power, which are costly, thus minimizing chances of success. The issue of electricity is paramount if Uganda is to develop into an industrial economy.

Lack of capital is another impediment to businesses in their early stages. Results of the study indicated a significant proportion of the respondents, 64(48%) raised this as a major problem. First, these businesses were started with limited capital. As observed by Snyder, 'do not think that you can get a million-shilling start-up loan for a business. Even if you have 500,000 shillings, you can start small, small.'[11] Secondly, microbusinesses lack collaterals such as cars or land titles that can be deposited to get loans from the traditional commercial banks. On the other hand, the loans provided by microfinance institutions are small, with a short repayment period and high interest rates. This is in line with Mbaguta's assertion that financing suitable for Small Medium Enterprises (SMEs) is still insufficient in Uganda, and this results in limited growth and survival of SMEs.[12]

Ssendaula lists factors that have discouraged banks from lending to SMEs.[13] Among them are poorly compiled records and accounts; low levels of technical and management skills; outdated technologies; lack of professionalism and networking; lack of collateral; lack of market outlets due to poor quality and non-standardized products; poor linkages and limited knowledge of business opportunities. In addition, most businesses, such as those dealing in foodstuffs, have been affected by lack of proper storage facilities. This has been a major limitation on business success because most agricultural products require preservation and have an inelastic demand meaning that even if their prices are lowered, quantity demanded can increase in that same proportion to clear the market of surpluses.

Lack of sales has been a predicament during the inception of such businesses. This is because most of these businesses lack the competence of challenging already established businesses. They usually lack a public image and yet publicity is one of the major mechanisms for business triumph. The study also revealed that these business people start enterprises without careful regard to the location of the business; thus less sales and less profits and this delays growth. With the above in mind, what should be done to increase sales?

Firstly, the owners and managers of smallscale enterprises must make form of market study so that the quality of the goods produced/services provided are what customers/clients want. However, most of the small scale businesses studied will find the market study costs to be prohibitive. Joining market groups can help. Secondly, the owners/managers must overcome any negative attitude/environment in service delivery that can put off customers/clients. Thirdly, the owners/managers of small business must understand the scope and use of marketing knowledge. Lastly, but important too, the small scale business will do well when the owners are present in the business to attend to customers and answer their queries.

The problem of pricing was prominent among the startup reasons of small scale business failure. Owners lack the capacity to ascertain best prices and they tended to operate at high prices in relation to already existing businesses**.** This tends to away most customers to their competitors who are already in the business and maneuver at lower costs.

The findings of the study revealed that the profitability of many businesses in their early stages is negative. During the startup period, negative cash flows have been a common characteristic, mostly due to lack of sales, pricing problems, high competition, and most often, operation on a small scale combined with soaring costs of operation.

Poor record keeping is also a cause for startup business failure. In most cases, this is not only due to the low priority attached by new and fresh entrepreneurs, but also a lack of the basic business management and skills. Most business people, therefore, end up losing track of their daily transactions and cannot account for their expenses and their profits at the end of the month. Biryabarema emphasizes the importance of proper record keeping in that it enables a small business to have accurate information on which to base decisions such as projecting sales and purchases or determining the break-even point and making a wide range of other financial analyses.[14] However, the persistent lack of proper records has seen the closure of some businesses, thereby making it a significant issue for business success.

During the early stages of some business start-ups, owners were unable to separate their business and family/domestic situations. Business funds were put to personal use and thus used in settling domestic issues. This has a negative impact on profitability and sustainability. Some owners/managers employ family members simply because of kinship relations. In some cases, these have turned out to be undisciplined and ineffectual, a factor that has led to eventual and sometimes rapid failure of businesses.

Lack of effective management during their early stages is also a major cause of business failure for small businesses. Owners tend to manage these businesses themselves as a measure of reducing operational costs. This study uncovered the example of businessperson who locks the shop for a full day whenever he goes shopping in Kampala. He does this once every week, a total of four days a month. One result of this is loss of customer loyalty. This is clearly explained by Katuntu's remarks that poor location of business, lack of management experience, and over-investment in fixed assets has led to the collapse of many businesses. [15]

During this research survey, faulty products were also identified as an additional startup problem. Since most new businesspersons are not experienced in the sector, they are not normally familiar with the condition of the products they purchase. Products which do not suit the tastes of the customers remain in stores thus tying up working capital.

Lack of planning (17%) was also listed as a cause of businesses failure during their startup phases. Less than a third (30%) prepare a formal business plan prior to starting up and 37% do not plan at all. The survey found that most businesses just start without plans. Small business persons end up with no set goals or targets to meet. The study also revealed that the cost for preparation of a simple business plan ranges from USD100-200. Small business owners looking for start up capital cannot manage this amount.

Respondents were also asked to identify any additional problems not specifically covered by the questionnaire. A number of causes were revealed by the study: competition, high rent charges, lack of business skills, transportation costs, and politics.

Once businesses are established, they confront competition from other businesses in either similar or related businesses. 112 (84 %) of respondents agreed. As towns expand, the number of entrepreneurs also increases. Therefore, the success of one business often comes at the expense of another. This necessitates advertising and price reductions so as to attract more customers, which in turn lead to a potential reduction of profitability.

High rental charges have impeded the success of many businesses as some charges are pegged to the United States dollar, which in most cases appreciates against the Uganda shilling. One businessperson mentioned that their rent is US$200 for a space of 12 feet by 10 feet. Expansion of towns has led to increased demand for business premises, which means that some small businesses have been pushed away from the busy areas of the town to the periphery. This has increased costs and resulted in poor sales and negative cash flow, thus minimizing the chances for most businesses to succeed.

High transport costs have become one of the problems faced by startup businesses. Lack of oil reserves in the country, coupled with the unstable Ugandan shilling, has made the cost of transport high and unpredictable. Fuel is a factor that propels an increase in costs of production across the board, which has led to failure of many businesses. Communication networks have also been poor, leading to high operation costs. Lack of information on existing goods and poor access roads in rural areas have constrained businesspersons to buy products that are in easy-to-reach areas where competition is relatively high.

Politics can also pose a threat to business success. Building and construction companies complain that tenders are awarded to political favorites who then do not deliver to the required standards. Some businesses operate without paying taxes or are under-assessed, gives them have an advantage over their competitors. Politics influences customers who choose to deal with specific people because they were in the same camp during presidential, parliamentary or local council elections, irrespective of the quality of the services provided. Gordon Wavamunno, who has built a vast business empire in a wide range of fields (including transport, manufacturing, tourism, motor vehicle distribution, trade, insurance and banking, commercial farming, electronic media and property development) has personally stated that politics and business are like fire and water – they do not exist together amicably.[16]

PRACTICAL ACTION AGAINST BUSINESS FAILURE

The interest of the researcher was to establish the causes of small business failure, either during the startup or those experienced once established, and how they might be overcome. From the study, the researcher came up with a number of approaches towards improving the management of small businesses not only in the Bushenyi and Mbarara towns of Uganda, but also further afield (see table 3).

Table 3: Practical action against business failure

Causes	Some practical measures
Lack of capital	• Make a budget; source cheap loans from financial institutions • Borrow from friends; negotiate favourable credit purchases • Negotiate advance payments from your customers • Merge with others that have similar businesses • Seek silent partners • Re-invest the profits made • Respect money by making frank spending priorities • Join Microfinance Institutions or Saving and Loan Associations
Increased taxes	• Tax assessment by local government in conjunction with the business owner • Business people should know the investment code and tax regulations • Pay tax in time to ease the burden
Low sales	• Location of the business premises is very important • Improving customer care • Employing qualified personnel and motivating them • Carrying out market research and advertising • Optimization of peak periods such as morning, lunch and evening hours
Management problems	• Financial management should be emphasized • Keeping records of workers to help in evaluation • Attending refresher courses on business management skills • Networking with other people with similar businesses or at professional level
Negative cash flow	• Scale down operational costs • Prepare a cost –benefit analysis • Lease equipment and other financial assets to improve your cash flow • Negotiate outstanding loans through payment procedures • Aggressively pursue the account receivables
Poor record keeping	• Employ qualified personnel and put them in position according to their skills • Establish a record of books of accounts on a daily, weekly, monthly and annual basis • Financial records should be a priority since they aid planning
Family situations	• Separate business activities and family obligations • Look for alternative sources of income to cater for family basic needs • Set aside the time to spend with the family for social events
Inadequate control of inventory	• Know and understand existing skills needed • Maintain, control and take stock of the inventory regularly
Lack of business plan	• Set specific targets • Prepare cash flow forecast and budgets
Faulty product concept	• Spot supervision during mixing of ingredients for businesses engaged in such businesses • Regular product inspection to protect against selling the defective product • Have an inspector on staff to inspect goods in process to protect against poor quality of the finished goods
Load shedding	• Purchase a generator

Source: A mix of respondents and author

For small businesses to succeed, it is essential to have a good business plan whether formal or informal. In addition, small businesses should aim at fixing prices that will enable them to earn sufficient profits for survival and growth. Further, every small businessperson needs effective and efficient management skills to go into business and new, effective, and efficient management skills to stay there.

CONCLUSION

Small businesses in Uganda are faced with a number of challenges that lead to business failure. These causes of failure are quite diverse in nature. They have resulted in more than fifty percent of businesses failing in the first five years and fighting an uphill battle from the start. The study established causes of small businesses failure, among which are: lack of business plans, high taxes, load shedding, lack of capital, poor market, high rent charges and wrong pricing. It came up with practical actions on how to overcome them. The aim is to help the business owners design business plans and work with one another. If followed, then businesses might move from where they are today to where their owners, investors and managers want them to be.

NOTES

1. This paper is based on data collected from Bushenyi and Mbarara towns during January 2003 to April 2003. Several people helped in collecting data most especially the 2002/2003 year III Bachelor of Development studies undergraduate students of Mbarara University of Science and Technology (MUST). Mr. Allen George formerly with the Faculty of Development Studies, MUST made comments on the draft research tools. Professor Owen Willis of Dalhousie University is thanked for comments on earlier drafts of this paper. The usual disclaimer applies; all remaining errors are mine.
2. The size of the service was halved; real wages increased from next to nothing to a broadly acceptable living wage, most allowances were consolidated and monetised into single cash. (http://www.Vuw.ac.nz)
3. Bagazonzya 2003. The population of Uganda according to the 2002 Population and Housing Census is 26.3 million people.
4. Small Business Act, 1953.
5. Mbaguta, 2002.
6. Bagazonzya 2003. The exchange rate to the US $1 = 1,860 Ugandan shillings.
7. Keogh 2002.
8. Uganda Bureau of Statistics, 2004.
9. Uganda Bureau of Statistics, 2003.
10. Mwanje 2003
11. Snyder, 2000.
12. Mbaguta, 2002.
13. Ssendaula, 2002.
14. Biryabarema, 1998.
15. This was contained in a seminar paper by the Executive Director of DFCU Bank, Mr Robert Katuntu in one day Seminar of the Institute of Certified Public Accountants of Uganda.
16. Wavamunno, 2000.

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